

G50L00
Maryland Supplemental Retirement Plans

Program Description

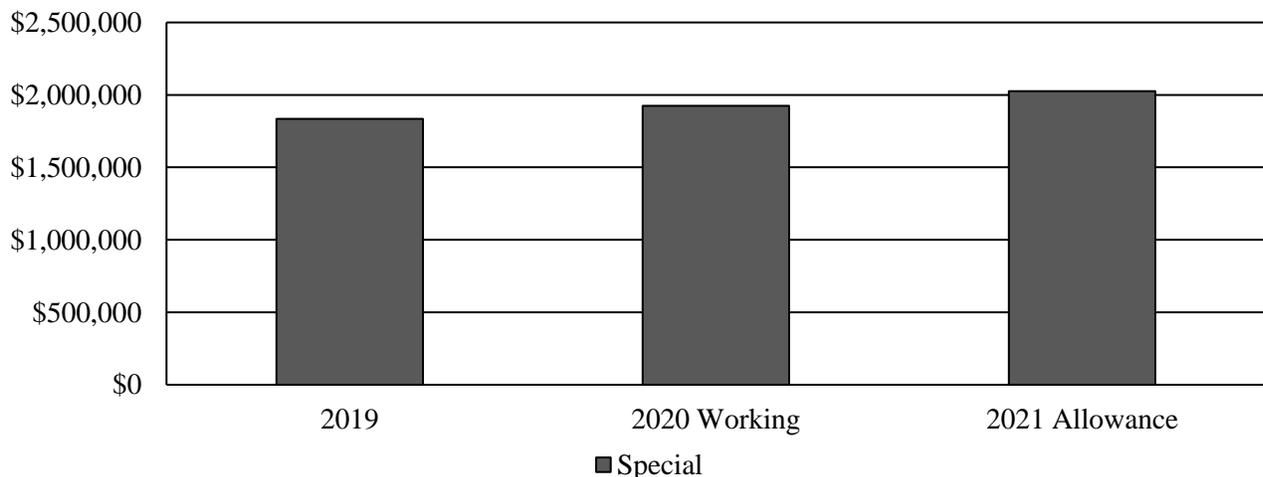
The Teachers’ and State Employees’ Supplemental Retirement Plans are administered by a board of trustees, as established in Title 35 of the State Personnel and Pensions Article. The board has responsibility over four plan options, which can be found in **Appendix 1**.

The Maryland Supplemental Retirement Plans (MSRP) staff supports the board of trustees’ work in selecting investment options and overseeing operations. MSRP staff also provides educational programs and information to State employees and human resources personnel. These efforts are designed to create awareness among State employees of the need and mechanisms available to save for their own retirement.

MSRP finances operations through a fee imposed on members’ accounts based on a percentage of assets in the plans and a flat-rate monthly charge. The board fee, effective October 1, 2019, is currently composed of a 0.0425% asset fee and a monthly per account charge of \$0.50 on every account with at least \$500 (except for 401(a) match plan accounts). The board contracts with Nationwide Retirement Solutions, Inc. (Nationwide) for plan administration. The Nationwide contract requires a management fee of 0.0775% of assets. Therefore, the reported total participant fee is 0.12% of plan assets and a \$0.50 charge on specified accounts on an annual basis.

Operating Budget Summary

Budget Increases \$99,817 or 5.2% to \$2.0 Million in Fiscal 2021



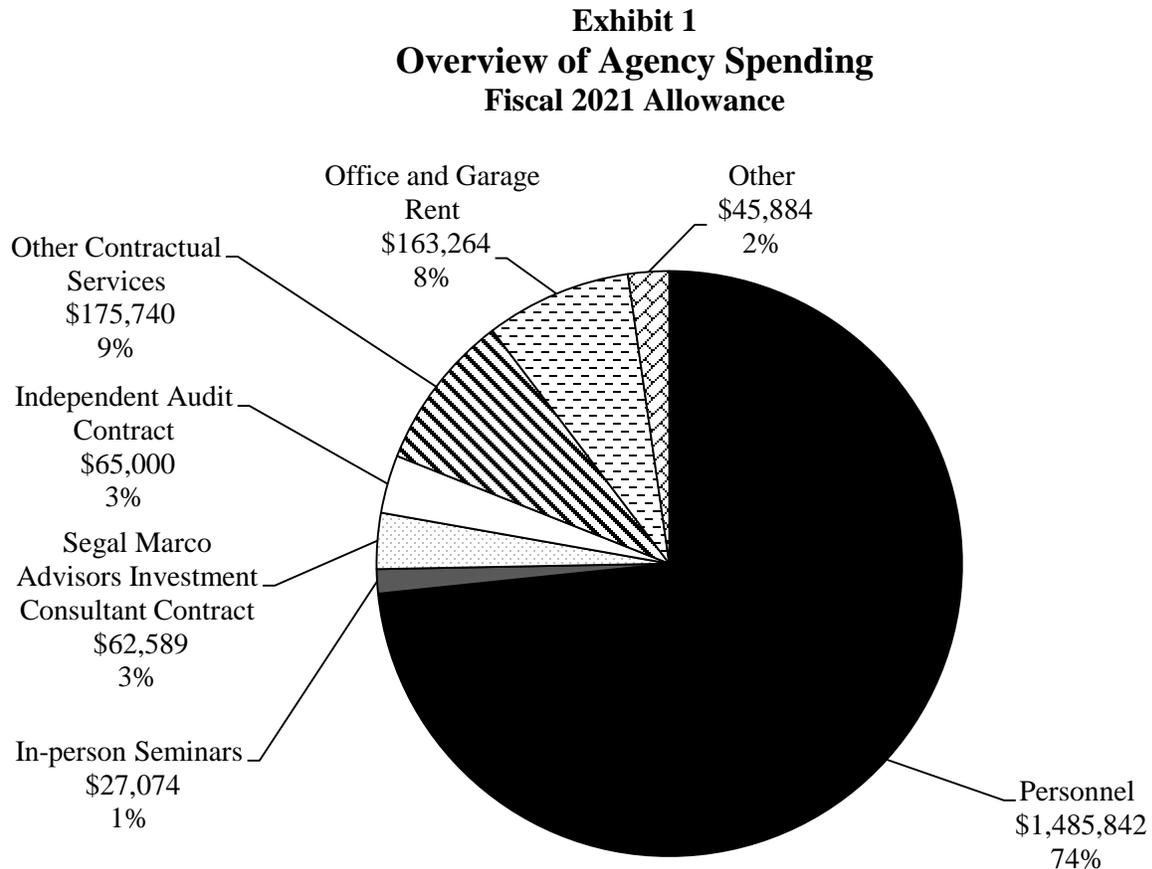
Note: Numbers may not sum due to rounding. The fiscal 2020 appropriation includes deficiencies, planned reversions, and general salary increases. The fiscal 2021 allowance includes contingent reductions and general salary increases.

For further information contact: Jason A. Kramer

Phone: (410) 946-5530

Fiscal 2021 Overview of Agency Spending

As shown in **Exhibit 1**, nearly three-quarters of MSRP’s fiscal 2021 allowance is for agency personnel costs. Other large costs include funding for office and garage leases (8.1%) and contractual services (14%). MSRP’s two largest contracts are for investment consulting with Segal Marco Advisors and for an independent audit.



Source: Governor’s Fiscal 2021 Budget Books

Proposed Budget Change

The fiscal 2021 allowance increases by \$99,817, or 5.2%, compared to the fiscal 2020 working appropriation, as shown in **Exhibit 2**. Including across-the-board general salary increases budgeted in the Department of Budget and Management, personnel costs at MSRP increase by \$48,379. Salary increases and the addition of 1 new position are offset by the reduction of approximately \$123,000 in fiscal 2020 one-time reclassification costs.

Exhibit 2
Proposed Budget
Maryland Supplemental Retirement Plans
(\$ in Thousands)

| How Much It Grows: | <u>Special Fund</u> | <u>Total</u> |
|-----------------------------------|----------------------------|---------------------|
| Fiscal 2019 Actual | \$1,836 | \$1,836 |
| Fiscal 2020 Working Appropriation | 1,926 | 1,926 |
| Fiscal 2021 Allowance | <u>2,025</u> | <u>2,025</u> |
| Fiscal 2020-2021 Amount Change | \$100 | \$100 |
| Fiscal 2020-2021 Percent Change | 5.2% | 5.2% |

| Where It Goes: | <u>Change</u> |
|--|----------------------|
| Personnel Expenses | |
| Regular compensation..... | \$74 |
| One new position | 52 |
| Retirement contributions..... | 26 |
| Fiscal 2021 2% general salary increase | 11 |
| Workers' compensation premium assessment | 6 |
| Social Security contributions | 5 |
| Fiscal 2020 1% general salary increase | 5 |
| Health insurance premiums..... | 5 |
| Turnover adjustments..... | -13 |
| Reclassification | -123 |
| Other Changes | |
| Statewide cost allocations and other contractual services..... | 23 |
| Segal Marco Advisors contract for investment consulting to better reflect fiscal 2019 actuals... | 21 |
| Other changes..... | 8 |
| Total | \$100 |

Note: Numbers may not sum due to rounding. The fiscal 2020 appropriation includes deficiencies, planned reversions, and general salary increases. The fiscal 2021 allowance includes contingent reductions and general salary increases.

Personnel Data

| | <u>FY 19</u> <u>Actual</u> | <u>FY 20</u> <u>Working</u> | <u>FY 21</u> <u>Allowance</u> | <u>FY 20-21</u> <u>Change</u> |
|------------------------|---|--|--|--|
| Regular Positions | 13.00 | 13.00 | 14.00 | 1.00 |
| Contractual FTEs | <u>0.00</u> | <u>0.00</u> | <u>0.00</u> | <u>0.00</u> |
| Total Personnel | 13.00 | 13.00 | 14.00 | 1.00 |

Vacancy Data: Regular Positions

| | | |
|--|------|-------|
| Turnover and Necessary Vacancies, Excluding New Positions | 0.14 | 1.08% |
| Positions and Percentage Vacant as of 12/31/19 | 1.00 | 7.69% |
| Vacancies Above Turnover | 0.86 | |

- MSRP has added 1 new position to carry out additional reporting and administrative responsibilities related to the implementation of Chapter 273 of 2019, which allows MSRP to offer community investment trusts (CIT) as an option to members. CITs are pooled investment vehicles, like mutual funds, but are offered by banks and trust companies. As such, they are not registered with the Securities and Exchange Commission based on an exemption from registration. CITs are only offered to certain types of investors, including qualified and eligible retirement plans, such as the MSRP 457 Plan, 401(k) Plan, and 401(a) Match Plan. The MSRP 403(b) Plan is not a permitted investor in a CIT because, under current federal law, 403(b) plans can only hold certain types of securities (annuity contracts and mutual funds). Because of these differences, CITs can be offered at a lower expense ratio.

Key Observations

1. Market Performance Leads to High Reserves in Fiscal 2019

As shown in **Exhibit 3**, MSRP options fell short of benchmarks in fiscal 2019 only over the most recent one year period; all other measured periods met or exceeded all annual average rates of return benchmarks. In the past five fiscal years, MSRP options have generally met or outperformed plan benchmarks.

Exhibit 3 Maryland Supplemental Retirement Average Rates of Return Fiscal 2015-2019

| | <u>1 Year</u> | <u>3 Years</u> | <u>5 Years</u> | <u>10 Years</u> |
|---|----------------------|-----------------------|-----------------------|------------------------|
| Annual Average Rates of Return as of June 30, 2019 | | | | |
| Maryland Supplemental Retirement Plans (MSRP) Options | 6.7% | 10.4% | 7.0% | 11.9% |
| Benchmark Indices | 6.8% | 10.4% | 7.0% | 10.5% |
| Annual Average Rates of Return as of June 30, 2018 | | | | |
| MSRP Options | 10.1% | 8.0% | 9.5% | 8.1% |
| Benchmark Indices | 9.8% | 7.9% | 9.2% | 7.7% |
| Annual Average Rates of Return as of June 30, 2017 | | | | |
| MSRP Options | 14.5% | 6.0% | 10.4% | 6.2% |
| Benchmark Indices | 14.1% | 5.9% | 10.2% | 5.7% |
| Annual Average Rates of Return as of June 30, 2016 | | | | |
| MSRP Options | -0.3% | 7.6% | 7.5% | 6.4% |
| Benchmark Indices | 0.5% | 7.6% | 7.6% | 6.1% |
| Annual Average Rates of Return as of June 30, 2015 | | | | |
| MSRP Options | 3.6% | 13.0% | 12.6% | 7.6% |
| Benchmark Indices | 3.8% | 12.7% | 12.6% | 7.0% |

Source: Maryland Supplemental Retirement Plans

G50L00 – Maryland Supplemental Retirement Plans

Exhibit 4 compares MSRP investment performance with benchmark indices as of September 2019. Two large cap stock funds – American Century Equity Growth and American Funds Growth – underperformed benchmark indices in all time periods. T. Rowe Price Mid-Cap Value also underperformed in all time periods. Underperformance of a fund may put a fund on watch but does not necessarily result in removal. Long-term performance is prioritized over short-term results.

Exhibit 4
MSRP Investment Performance Compared with Benchmark Indices
As of September 2019

| | <u>1-year</u> | <u>3-year</u> | <u>5-year</u> | <u>10-year</u> |
|---|---------------|---------------|---------------|----------------|
| Bond Funds | | | | |
| TCW Core Fixed Income Fund I | ✓ | ✓ | ✗ | ✓ |
| Balanced Funds | | | | |
| Fidelity Puritan Fund | ✗ | ✗ | ✗ | ✓ |
| T. Rowe Price Retirement Balanced | ✗ | ✗ | ✗ | ✓ |
| Large Cap Stock Funds | | | | |
| Parnassus Core Equity | ✓ | ✓ | ✓ | ✓ |
| American Century Equity Growth | ✗ | ✗ | ✗ | ✗ |
| American Funds Growth | ✗ | ✗ | ✗ | ✗ |
| Delaware Value Fund Institutional Class | ✗ | ✗ | ✓ | ✓ |
| Mid Cap Stock Funds | | | | |
| Janus Enterprise N | ✓ | ✓ | ✓ | - |
| T. Rowe Price Mid-Cap Value | ✗ | ✗ | ✗ | ✗ |
| Small Cap Stock Fund | | | | |
| T. Rowe Price Small Cap Stock | ✓ | ✓ | ✓ | ✓ |
| International Stock Fund | | | | |
| American Funds Euro Pacific Growth | ✓ | ✓ | ✓ | ✓ |

MSRP: Maryland Supplemental Retirement Plans

✓ Fund equaled or beat benchmark index.

✗ Fund underperformed benchmark index.

Source: Maryland Supplemental Retirement Plans; Segal Advisors

G50L00 – Maryland Supplemental Retirement Plans

In recent years, a run up in financial markets and settlements caused MSRP revenues to increase at a faster pace than expenditures, resulting in substantial fund balances in excess of the board of trustees' target of 25% of operating expenses. The board responded with fee holidays in calendar 2013 to 2016. The last asset fee holiday was from January to June 2018. **Exhibit 5** shows the plans' assets, participant fees, and the agency's operating budget from fiscal 2014 to 2020.

At the end of fiscal 2019, the board of trustees had a reserve fund equal to 70% of the annual appropriation, nearly double the fund balance target of 25%. The board has permanently reduced asset fees from 0.05% to 0.0425%, effective October 1, 2019, and believes that will be sufficient to reduce the reserve balance and that there is no need for fee holidays. However, at current asset levels, the fee reduction would only reduce revenue from the fee by approximately \$200,000 per year. **The Department of Legislative Services recommends that MSRP explain why a larger fee reduction or fee holidays are not warranted.**

Exhibit 5
Assets and Participants' Fees and Operating Budget
Fiscal 2014-2020 Est.

| | <u>2014</u> | <u>2015</u> | <u>2016</u> | <u>2017</u> | <u>2018</u> | <u>2019</u> | <u>2020 Est.</u> |
|--|--------------------|--------------------|--------------------|--------------------|--------------------|--------------------|--------------------|
| Net Total Assets (\$ in Billions) | \$3.33 | \$3.42 | \$3.38 | \$3.74 | \$4.02 | \$4.17 | \$4.20 |
| Plan Administrator Fees | \$2,726,532 | \$2,941,840 | \$2,807,945 | \$3,102,426 | \$4,055,312 | \$3,697,123 | \$4,293,000 |
| As Percent of Assets | 0.08% | 0.09% | 0.08% | 0.08% | 0.10% | 0.09% | 0.10% |
| Board Asset Fee | \$922,149 | \$1,107,118 | \$1,080,654 | \$1,755,171 | \$1,055,427 | \$1,976,369 | \$1,975,000 |
| As Percent of Assets* | 0.03% | 0.03% | 0.03% | 0.05% | 0.03% | 0.05% | 0.05% |
| \$0.50 Monthly Charge Per Account | 360,231 | 359,090 | 362,942 | 366,465 | 370,090 | 229,461 | 373,000 |
| One-time Settlement Revenue | | 13,660 | | 122,406 | 69,765 | 0 | 0 |
| Adjustment for Timing Differences** | -68 | 131,498 | 9,939 | -17,007 | 0 | 143,175 | 0 |
| Total Board Revenue | \$1,282,312 | \$1,611,366 | \$1,453,535 | \$2,227,035 | \$1,495,282 | \$2,349,005 | \$2,348,000 |
| Operating Expenses | \$1,521,864 | \$1,666,333 | \$1,673,956 | \$1,782,930 | \$2,016,003 | \$1,807,147 | \$1,856,662 |
| Adjustment for Timing Differences** | 2,212 | -13,941 | -3,600 | 142 | 00 | 2,499 | 00 |
| Total Operating Expenses | \$1,524,076 | \$1,652,392 | \$1,670,356 | \$1,783,072 | \$2,016,003 | \$1,809,646 | \$1,856,662 |
| Carryover Balance | \$609,722 | \$568,696 | \$351,875 | \$795,838 | \$275,116 | \$814,475 | \$1,305,813 |
| Carryover Balance as Percent of Operating Expenses | 40.0% | 34.4% | 21.1% | 44.6% | 13.6% | 45.0% | 70.3% |

* The board asset fee percentage is less than 0.05% from fiscal 2014 to 2016 and in fiscal 2018 as a result of fee holidays.

** Timing adjustment is needed to align with Financial Management Information System accounting. Expenditures are budgeted on a fiscal year, while plans and revenues are on calendar years.

Source: Maryland Supplemental Retirement Plans

Operating Budget Recommended Actions

1. Concur with Governor's allowance.

Updates

- **No Growth in Number of Contributing Members:** As shown in **Exhibit 6**, plan membership continues to grow, while the number of contributing members remains flat.
-

Exhibit 6
Maryland Supplemental Retirement Plans Members and Contributing Members
Fiscal 2011-2019

| <u>Fiscal Year</u> | <u>Total Members</u> | <u>% Change</u> | <u>% Eligible</u> | <u>Contributing Members</u> | <u>% Change</u> | <u>% Eligible</u> |
|--------------------|----------------------|-----------------|-------------------|-----------------------------|-----------------|-------------------|
| 2011 | 58,993 | | 75% | 36,184 | | 46% |
| 2012 | 58,121 | -1.5% | 76% | 35,263 | -2.5% | 46% |
| 2013 | 57,477 | -1.1% | 74% | 34,373 | -2.5% | 44% |
| 2014 | 57,486 | 0.0% | 74% | 33,932 | -1.3% | 44% |
| 2015 | 58,311 | 1.4% | 74% | 34,302 | 1.1% | 44% |
| 2016 | 59,144 | 1.4% | 76% | 34,175 | -0.4% | 44% |
| 2017 | 59,632 | 0.8% | 77% | 34,219 | 0.1% | 44% |
| 2018 | 60,696 | 2.6% | 78% | 34,278 | 0.3% | 44% |
| 2019 | 61,703 | 3.5% | 79% | 34,214 | 0.0% | 44% |

Source: Governor's Fiscal 2021 Budget Books

Appendix 1
Teachers’ and State Employees’ Supplemental Retirement Plans
Plan Characteristics
Calendar 2019

| <u>Plan Characteristic</u> | <u>401(k)</u> | <u>457(b)</u> | <u>403(b)</u> |
|--|--|--------------------------------------|--|
| Participation | State employees | State employees | Employees of State educational institutions |
| Contribution Option | Tax-deferred; after-tax Roth | Tax-deferred; after-tax Roth | Tax-deferred |
| Contribution Limit | \$19,000 | \$19,000 | \$19,000 |
| Catch-up Provision for Employees Over 50 | \$6,000 | \$6,000 | \$6,000 |
| Withdrawal While Employed | Age 59.5, or hardship | Age 70.5, or unforeseeable emergency | Age 59.5, or hardship |
| Avoid 10% Premature Withdrawal Penalty | Leave State employment at age 55 or older, or at age 59.5 regardless of employment | Leaving State employment | Leave State employment at age 55 or older, or at age 59.5 regardless of employment |

Source: Maryland Supplemental Retirement Plans

- Tax-deferred plans mean that the account may grow by additional contributions and investment earnings without paying income taxes until those amounts are withdrawn from the plans.
- Since April 2011, after-tax Roth contributions are permitted into 457(b) and 401(k) plans directly from payroll, which means that no further taxes will be due on these contributions or earnings on eligible payouts from the plans.
- When participating in both a 457(b) and 401(k) plan, or participating in both a 457(b) and 403(b) plan, a member may contribute up to the maximum annual contribution limit (\$19,000) to each plan, for a total of \$38,000 annually.
- If a member is participating in both the 401(k) and 403(b) plan, a member may not contribute higher than \$19,000 (or \$25,000 if using the age 50 catch-up provision) annually.
- The State matching program under Internal Revenue Code Section 401(a) provided to eligible employees’ 457(b), 401(k), and 403(b) plans has been suspended since fiscal 2010.

**Appendix 2
Object/Fund Difference Report
Maryland Supplemental Retirement Plans**

| <u>Object/Fund</u> | <u>FY 19 Actual</u> | <u>FY 20 Working Appropriation</u> | <u>FY 21 Allowance</u> | <u>FY 20 - FY 21 Amount Change</u> | <u>Percent Change</u> |
|-------------------------------|-------------------------|--|----------------------------|--|---------------------------|
| Positions | | | | | |
| 01 Regular | 13.00 | 13.00 | 14.00 | 1.00 | 7.7% |
| Total Positions | 13.00 | 13.00 | 14.00 | 1.00 | 7.7% |
| Objects | | | | | |
| 01 Salaries and Wages | \$ 1,336,868 | \$ 1,428,667 | \$ 1,461,044 | \$ 32,377 | 2.3% |
| 02 Technical and Special Fees | 0 | 3,850 | 3,850 | 0 | 0% |
| 03 Communication | 26,373 | 6,250 | 6,250 | 0 | 0% |
| 04 Travel | 22,649 | 27,074 | 27,074 | 0 | 0% |
| 07 Motor Vehicles | 10,920 | 11,760 | 11,760 | 0 | 0% |
| 08 Contractual Services | 261,895 | 259,288 | 303,329 | 44,041 | 17.0% |
| 09 Supplies and Materials | 14,422 | 15,407 | 17,500 | 2,093 | 13.6% |
| 10 Equipment – Replacement | 4,349 | 0 | 0 | 0 | 0.0% |
| 11 Equipment – Additional | 7,458 | 12,885 | 12,885 | 0 | 0% |
| 13 Fixed Charges | 150,681 | 155,449 | 160,740 | 5,291 | 3.4% |
| Total Objects | \$ 1,835,615 | \$ 1,920,630 | \$ 2,004,432 | \$ 83,802 | 4.4% |
| Funds | | | | | |
| 03 Special Fund | \$ 1,835,615 | \$ 1,920,630 | \$ 2,004,432 | \$ 83,802 | 4.4% |
| Total Funds | \$ 1,835,615 | \$ 1,920,630 | \$ 2,004,432 | \$ 83,802 | 4.4% |

Note: The fiscal 2020 appropriation does not include deficiencies, planned reversions, or general salary increases. The fiscal 2021 allowance does not include contingent reductions or general salary increases.